

Message Text

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ACTION EUR-12

INFO OCT-01 EA-10 IO-13 ISO-00 CIAE-00 DODE-00 PM-05
H-01 INR-10 L-03 NSAE-00 NSC-05 PA-01 SP-02
SS-15 ICA-11 EB-08 COME-00 TRSE-00 OMB-01 /098 W
-----058732 091107Z /12

R 061707Z SEP 78
FM AMEMBASSY COPENHAGEN
TO SECSTATE WASHDC 7120
INFO AMEMBASSY ANKARA
AMEMBASSY ATHENS
AMEMBASSY BERN
AMEMBASSY CANBERRA
AMEMBASSY HELSINKI
AMEMBASSY LISBON
AMEMBASSY MADRI
AMEMBASSY OSLO
AMEMBASSY OTTAWA
AMEMBASSY REYKJAVIK
AMEMBASSY STOCKHOLM
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E.O. 11652: NA/S
TAGS: EGEN DA
SUBJECT: NEW GOVERNMENT WINS PASSAGE OF TAX AND PRICE CONTROL
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LEGISLATION

REF: A. COPENHAGEN 5698 AND B. COPENHAGEN 5781 (NOTAL)

SUMMARY: THE PARLIAMENT RECESSED TODAY SEPTEMBER 8 UNTIL THE MEETING
OF THE REGULAR FALL SESSION ON OCTOBER 3, HAVING ADOPTED AN INCREASE
IN THE VAT FROM 18 TO 20.25 PERCENT, TEMPORARY PRICE FREEZES FOR THE

PERIOD UNTIL MARCH 1, 1979, AND A NUMBER OF BILLS TO COMPENSATE SOCIAL BENEFICIARIES FOR THE TAX INCREASE. THE NEW GOVERNMENT SUCCESSFULLY BEAT OFF THE FIRST CHALLENGE TO ITS PROGRAM. END SUMMARY.

1. THE PARLIAMENT ADOPTED TODAY SEPTEMBER 8 THE TWO BILL WHICH REPRESENT THE IMMEDIATE ECONOMIC RESTRAINT MEASURES OF THE NEW COALITION GOVERNMENT'S ECONOMIC PROGRAM. (A) AN INCREASE IN THE VALUE-ADDED TAX (VAT) FROM 18 TO 20.25 PERCENT (RATHER THAN 20-PERCENT AS ORIGINALLY PROPOSED) TO BE EFFECTIVE FROM OCTOBER 1, 1978 AND (B) A TEMPORARY PRICE FREEZE FOR THE PERIOD UNTIL MARCH 1, 1979, WHICH WILL, INDIRECTLY, ALSO AFFECT WAGE DRIFT. IN ADDITION, THE PARLIAMENT ADOPTED A NUMBER OF EXCISE TAX AMENDMENT BILLS OF A PURELY TECHNICAL NATURE (ADJUSTMENTS TO THE NEW VAT RATE WHERE VAT AND SPOT TAXES ARE TIED TOGETHER) AND SEVERAL SOCIAL SECURITY AMENDMENT BILLS TO ADJUST SOCIAL BENEFITS TO PROVIDE COMPENSATION FOR THE VAT INCREASE.

2. AS REPORTED REFTEL A PARA 2, THE GOVERNMENT'S VAT INCREASE BILL WAS NOT ORIGINALLY ACCOMPANIED BY SOCIAL BENEFIT ADJUSTMENTS AS HAS BEEN THE TRADITION IN ORDER TO MITIGATE THE REGRESSIVE EFFECTS OF THIS MAJOR INDIRECT TAX ON THE LOWEST INCOME GROUPS. THIS DEPARTURE FROM AN ESTABLISHED PRINCIPLE WAS PROBABLY MOTIVATED BY THE SIGNIFICANT IMPROVEMENTS IN SOCIAL SECURITY BENEFITS ADOPTED LAST MAY 31 (INITIAL SUPPLEMENTARY PENSION BENEFITS PAYABLE FROM JANUARY 1, 1979 PAID FROM THE SPECIAL SOCIAL SECURITY FUND ACCUMULATED LIMITED OFFICIAL USE

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NOTE BY OC/T: MESSAGE DELAYED IN TRANSMISSION.

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SINCE 1971). HOWEVER, THE ABSENCE OF TRADITIONAL COMPENSATORY LEGISLATION IN CONNECTION WITH THE PROPOSED VAT INCREASE PROVIDED AMMUNITION FOR THE GOVERNMENT'S OPPONENTS, (BOTH IN AND OUT OF THE LIMITED OFFICIAL USE

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COALITION PARTIES). A FAIRLY LARGE GROUP OF SOCIAL DEMOCRATIC PARLIAMENTARIANS, INCLUDING MANY WHO HAD OTHERWISE ACCEPTED THE COALITION WITH THE LIBERALS, TOOK EXCEPTION TO THE ALLEGEDLY REGRESSIVE NATURE OF THE NEW GOVERNMENT'S VERY FIRST LEGISLATIVE MEASURE. DURING READING OF THE BILL IT BECAME CLEAR THAT IT WOULD HAVE LESS SMOOTH SAILING THAN THE GOVERNMENT HAD EXPECTED AND THAT A MAJORITY AGAINST THE BILL WAS QUITE PROBABLE.

3. FACING POSSIBLE DEFEAT ON ITS INITIAL PROPOSAL, THE GOVERNMENT BOWED TO THE PRESSURE AND SUBMITTED BILLS TO ADJUST VARIOUS SOCIAL BENEFITS (OLD-AGE AND SURVIVORS, DISABILITY, AND FAMILY ALLOWANCES). THE LIBERAL COALITION PARTNERS INSISTED, HOWEVER, THAT THE ORIGINAL FISCAL RESTRAINT TARGET BE MAINTAINED BY RAISING THE PROPOSED VAT RATE FROM 20 TO 20.25 PERCENT. SINCE MANY OF THE SOCIAL BENEFIT ADJUSTMENTS WERE NOMINAL AND THEIR TOTAL COST WOULD REDUCE THE NET FISCAL VALUE OF THE VAT INCREASE ONLY FROM 3.2 TO 2.8 BILLION KRONER, IT IS CLEAR THAT PRINCIPLES RATHER THAN GENUINE FISCAL CONSIDERATIONS WERE PARAMOUNT. THE GOVERNMENT MAINTAINED ITS PROPOSAL FOR THE FURTHER VAT INCREASE EVEN IN THE FACE OF

VERY SHARP AND WIDE SPREAD OPPOSITION IN PARLIAMENT. THE ODD VAT-RATE INCIDENTALLY, ALSO CRITICIZED FOR THE COMPLICATED CALCULATIONS IT WOULD REQUIRE IN COMMERCIAL TRANSACTIONS.

4. IN THE VOTE ADDING THE EXTRA 0.25 PERCENT TO INITIAL BILL INCREASING THE TAX BY 2-PERCENT, A NARROW MARGIN OF 86 VOTES TO 84 VOTES CARRIED IT, BUT ONLY BECAUSE TWO MEMBERS OF THE CHRISTIAN PEOPLES' PARTY ABSENTED THEMSELVES FROM THE ROLL CALL, TO AVOID A DEFEAT FOR THE NEW GOVERNMENT. THE VAT-BILL INCREASING THE TAX TO 20.25 PERCENT PASSED AFTERWARDS BY A COMFORTABLE 94 TO 70 MAJORITY.

5. THE TEMPORARY PRICE FREEZE WAS NEVER REALLY IN QUESTION. IT WAS ADOPTED BY A 91 TO 70 MAJORITY (RADICAL LIBERALS LIMITED OFFICIAL USE

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ABSTAINED). THE SOCIAL COMPENSATORY BILLS WERE UNANIMOUSLY ADOPTED, EXCEPT THE INCREASE IN THE FAMILY ALLOWANCE WHICH WAS OPPOSED BY THE PROGRESSIVES (THE GLISTRUP PARTY).

6. COMMENT: THE D:S COALITION WEATHERED ITS FIRST TRIAL IN COMPARATIVELY GOOD SHPAE AFTER BUFFETING, NOT ONLY FROM BALKING LEFT-WING SOCIAL DEMOCRATS, BUT MEMBERS OF OTHER PARTIES OF THE CENTER-RIGHT AS WELL.

7. BUT THE RELIANCE ON ABSENCE OF TWO MEMBERS OF THE CHRISTIAN PARTY TO ADOPT LEGISLATION SHOWS THAT THE COALITION COULD BE VULNERABLE.

8. IN THE ABSENCE OF SOCIAL DEMOCRATIC UNITY. THE PRIME MINISTER WILL ATTEMPT TO OBTAIN UNITY ASSURANCES AT A SEPTEMBER 9 SPECIAL MEETING OF THE MAIN BOARD OF THE PARTY WHICH IS SCHEDULED FOR JUST THIS PRUPOSE.
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